Thailand

Vigorous growth in private consumption and investment contributed to a strong economic recovery in 2010, though growth will moderate this year and next, reflecting more subdued external demand and a base effect. Inflation is forecast to be higher this year, prompting the central bank to maintain a tightening monetary stance. In the social arena, the government is drawing up programs to address differences of income and opportunity, including a stronger social safety net and investment in transport infrastructure.

Economic performance

A strong recovery from a contraction in 2009 propelled GDP growth to 7.8% in 2010. Rebounding demand for exports spurred a pickup in manufacturing and bolstered both consumer and business confidence. Political tensions that led to 7 weeks of violent demonstrations in central Bangkok during April and May 2010 had a limited and temporary impact on economic recovery.

The biggest contributor on the demand side came from a bounce in investment, which added 5.2 percentage points of GDP growth (Figure 3.30.1). Investment had slumped in 2009 and been slack for several years before that.

Private fixed investment grew by 13.8% in 2010, mainly in export-oriented manufacturing. As export orders picked up, higher capacity utilization in industries such as automobiles and electrical machinery prompted investment in new equipment, which rose by 14.7% for the year. Private construction expanded by 10.6%, supported by low interest rates.

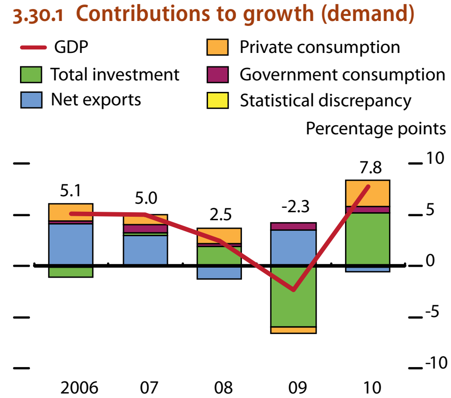
Private consumption, which had also declined in 2009, rose by 4.8% last year and contributed 2.5 percentage points to GDP growth. Its rise was assisted by a strengthening of the labor market and higher farm incomes, owing to increases in prices for agricultural commodities. Consumer sentiment weakened in the second quarter when the violence broke out, but it recovered after that.

Public consumption spending also contributed to economic growth as the government continued to disburse the fiscal stimulus measures initiated in 2009.

Public fixed investment in 2010 was slightly below prior-year levels. Lower investment from the budget and by state-owned companies was partly offset by outlays on the Thai Khem Kaeng (Strong Thailand) infrastructure program. This program, involving projects that could cost more than $40 billion over 3 years, started in October 2009. Of B350 billion ($10.2 billion) budgeted to be spent on infrastructure last year, about 74% was disbursed, after some delays during the political unrest in the first half.

This chapter was written by Luxmon Attapich of the Thailand Resident Mission, ADB, Bangkok.

3.30.1 Contributions to growth (demand)



Source: National Economic and Social Development Board. http://www.nesdb.go.th (accessed 11 March 2011).

Click here for figure data

On the supply side, industry generated most of the GDP growth. Manufacturing production surged by about 20% in the first half, then moderated to 8% growth in the second because of a base effect and softer global demand. Automobile production jumped by about 60% owing to a rebound in both domestic and export demand. Manufacturing contributed 5.4 percentage points of GDP growth, and industry as a whole added 6.0 percentage points.

Services contributed about 2 percentage points to total growth. Hotel and restaurant services expanded by 8.4%, supported by a pickup in tourism in the second half (arrivals had fallen during the protests in the capital—Figure 3.30.2). Tourist arrivals for the full year rose by 11.7% from 2009. Financial services grew by 8%, in line with expansion of business and consumer credit.

Agriculture, though, had another bad year because of drought, followed by floods. The sector contracted by 2.2%. Production fell for cassava, corn, fruit, palm oil, sugarcane, and rice.

Interruptions to food supplies caused by the bad weather added to inflation pressures induced by rising global prices for commodities and oil and stronger domestic demand. The consumer price index rose by 3.2% on average in 2010, after a period of deflation in 2009 (Figure 3.30.3). A 9.6% appreciation of the baht against the US dollar last year helped to temper the impact of rising import prices.

As economic recovery gained traction and the political situation settled in the second half of 2010, the Bank of Thailand started to normalize its policy interest rate (it had lowered the rate by 250 basis points to 1.25% during the global crisis). The central bank raised the rate five times between July 2010 and March 2011 (Figure 3.30.4) to 2.5% (still below the inflation rate).

Lending by commercial banks increased by 11.3% in 2010 (it had contracted by 1.8% in 2009), as business and consumer confidence improved, banks became more confident about the economy, and interest rates remained relatively low.

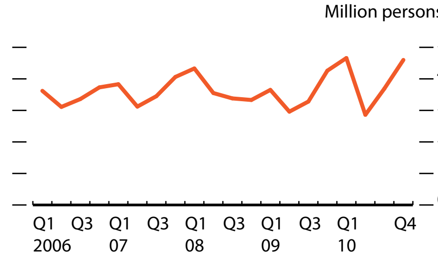
External trade rebounded (Figure 3.30.5). Merchandise exports rose by 28.5% to $193.7 billion, reflecting strong external demand for both agricultural and manufactured goods. Shipments of manufactured items, including autos and components, computers, electrical appliances, and machinery, rose by about 31%, agricultural products by 36%.

By destination, exports to the People's Republic of China, India, and Southeast Asia all jumped by about 35%, while those to major industrial economies (the European Union, Japan, and the United States) together rose by nearly 24%.

Recovery in domestic and external demand caused a near 37% surge in imports to $179.6 billion in 2010. Imports of raw materials and intermediate goods needed for export-oriented industries shot up by 42%, and the recovery in investment drove a 27.7% rise in imports of capital goods. Higher prices for imported oil added to the import bill. Surging imports brought down the merchandise trade surplus to $14.0 billion.

After taking into account a larger surplus in services, countered by a wider income deficit, the current account was in surplus equivalent to 4.7% of GDP. The capital and financial account recorded a net inflow of $15.6 billion.

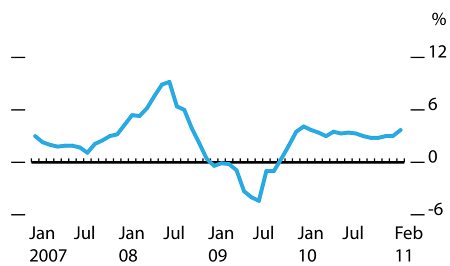
3.30.2 Tourist arrivals



Source: Bank of Thailand, available http://www.bot.or.th (accessed 28 March 2011).

Click here for figure data

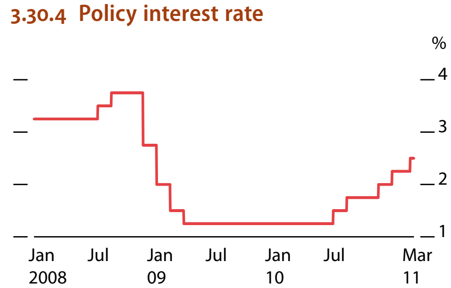
3.30.3 Monthly inflation



Source: CEIC Data Company; Bureau of Trade and Economic Indices. http://www.price.moc.go.th (both accessed 28 March 2011).

Click here for figure data

3.30.4 Policy interest rate



Source: Bloomberg (accessed 20 March 2011).

Click here for figure data

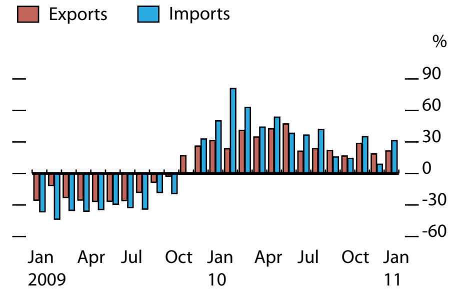
Current account surpluses and buoyant capital inflows into equity and debt securities ($55.2 billion in 2010) fueled the appreciation of the baht. To reduce that upward pressure, the Bank of Thailand liberalized restrictions on capital outflows, and the finance ministry removed a withholding tax waiver on bonds held by foreigners.

Foreign currency reserves rose by 24% to $165.7 billion in 2010, reflecting surpluses in the current, capital, and financial accounts as well as central bank purchases of foreign exchange to manage upward pressure on the baht. Reserves were equivalent to 9.5 months of imports of goods and services.

The government trimmed its budget expenditure in FY2010 (ending 30 September 2010) although total public spending increased, taking into account both on-budget and off-budget spending under the Thai Khem Kaeng program. Revenue collection was stronger than expected and exceeded the target by 10%, reining in the fiscal deficit to 2.1% of GDP from 4.8% in FY2009.

Public debt as a ratio to GDP fell to 42.5% at end-2010 from 43.9% in 2009, mainly the result of the larger GDP in 2010.

3.30.5 Merchandise trade growth



Source: Bank of Thailand. http://www.bot.or.th (accessed 28 March 2011).

Click here for figure data

Economic prospects

The government has indicated that national elections will be held in June 2011. Forecasts assume that the elections go smoothly and there are no serious disruptions that affect the economy.

Last year's strong rebound in GDP came from a low base brought about by the economic contraction in 2009. Consequently, economic growth will moderate considerably in 2011. Moreover, expected slower growth in major trading partners—the PRC, Southeast Asian neighbors, and major industrial countries—will damp the expansion in Thailand, as will the substantially higher cost of imported oil.

Merchandise exports are projected to increase by about 13% in nominal terms this year, less than half the rebound pace of 2010.

Private fixed investment is seen growing by about 9% in real terms, also below last year's pace. Capacity utilization rates suggest that some manufacturers will need to expand facilities to accommodate expected increases in domestic and external demand. Appreciation of the exchange rate has lowered the cost of imported machinery and equipment. Additionally, relatively low interest rates are conducive for investment.

An index of business sentiment in January 2011 indicated that business managers were confident about the outlook for orders and production, although they were concerned about rising costs.

Private consumption is forecast to grow by about 4% in real terms, due to growth in incomes. That marks a deceleration from 2010 but would still make a solid contribution to GDP growth. The labor market has tightened (businesses complain that they face difficulties in recruiting both skilled and unskilled labor), so that wages will likely increase.

Further, the government has said that it plans to raise minimum wages by 25% over 2 years if reelected, which would be on top of an increase in minimum wages in late 2010. Most government employees received a 5% wage increase from April 2011. Rural incomes are benefiting from high prices for many agricultural commodities.

3.30.1 Selected economic indicators (%)

	2011	2012
GDP growth	4.5	4.8
Inflation	3.5	3.0
Current account balance (share of GDP)	2.0	1.0

Source: ADB estimates.

A new round of concessions for low-income households will also support consumption. The government unveiled in January 2011 a package of "new year's gifts" that included subsidies on cooking gas, diesel fuel, electricity, and public transport. The authorities have extended price controls on a range of food staples and animal feeds and directed state banks to set aside B5 billion ($166 million) for low-interest loans to taxi drivers and street vendors, who might otherwise find it difficult to borrow because they are not salary earners and do not have collateral. Unsurprisingly, consumer confidence is buoyant (Figure 3.30.6).

While fiscal policy is expected to be mildly expansionary in the forecast period, monetary policy seems set to continue tightening. The government has budgeted to increase spending in FY2011 by about 22%, and widened the deficit target to 4% of GDP. Budget disbursements in the fiscal first quarter exceeded the target for that period. The rest of the Thai Khem Kaeng program will be funded through the budget, rather than mainly by off-budget expenditure as was the case last fiscal year. The fiscal deficit is expected to narrow to 3.2% in FY2012.

The Bank of Thailand is likely to gradually raise interest rates further during the forecast period and it will probably allow a gradual appreciation of the baht to help keep imported inflation in check.

Taking into account the outlook for domestic and external demand, the base effect, and the policy stance, GDP is forecast to grow by 4.5% in 2011 and 4.8% in 2012 (Figure 3.30.7).

Inflation was 3.0% in the first 2 months of 2011. Domestic food prices climbed, partly a result of bad weather. Higher global food and oil prices are adding to price pressures, but the subsidies and price controls should alleviate the impact of inflation on low-income households. For all 2011, inflation is forecast at 3.5% (Figure 3.30.8). It will ease next year, if global food and oil prices decelerate and the policy stance tightens as anticipated.

Volatile capital inflows are expected to ease this year. To manage the flows the central bank is likely to focus on relaxing rules for overseas investment and hedging by domestic businesses, rather than on controls on inflows.

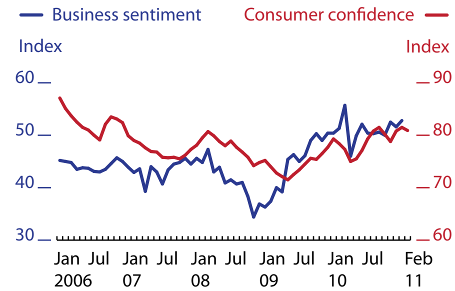
Higher prices for imported commodities and oil will likely mean that merchandise imports outpace exports in the forecast period. The trade surplus will decline slightly and the current account surplus is seen subsiding to about 2.0% of GDP in 2011 and 1.0% in 2012. Tourism, an important contributor to the surplus in services trade, got off to a good start in January 2011, when arrivals rose by 11.6% from the prior-year period.

Domestic risks to the outlook center on political uncertainty, which can have an impact on business and consumer confidence, and further bouts of bad weather (the south of the country saw extensive flooding in March 2011), which may reduce economic growth.

Development challenges

Political unrest over recent years, culminating in last year's violent demonstrations, has brought into focus gaps in incomes and opportunities in Thailand. The richest 20% of households account for

3.30.6 Confidence indicators

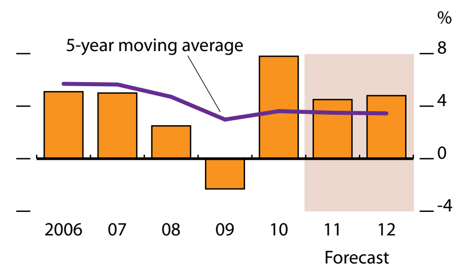


Note: A reading of less than 50 for business sentiment and less than 100 for consumer confidence denotes a deterioration.

Sources: Center for Economic and Business Forecasting; Bank of Thailand, http://www.bot.or.th (both accessed 28 March 2011).

Click here for figure data

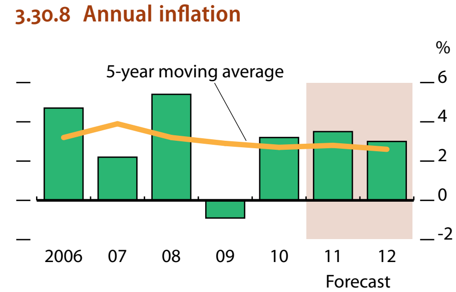
3.30.7 GDP growth



Source: Asian Development Outlook database.

Click here for figure data

3.30.8 Annual inflation



Source: Asian Development Outlook database.

Click here for figure data

nearly half of total household incomes and the Gini coefficient, a measure of income inequality, for the country is high at 0.51 (where 0 is perfect equality and 1 is absolute inequality).

Tackling regional inequality, the government is ramping up investment in transport infrastructure (roads, rail, and ports), which should encourage businesses to expand and generate employment outside the Bangkok area in the longer term. Faster decentralization should be used alongside this investment boost, giving local governments greater authority to make decisions over infrastructure and services to attract development to their areas as well as the fiscal resources to support this responsibility. (A decentralization act was passed in 1999, but implementation has lagged.)

Another government approach to mitigating inequality is to build a stronger social safety net. The draft 11th National Plan (2012–2016), to be finalized this year, includes a strategy to create a more equitable society. Based on this strategy, the government is setting up a voluntary pension fund for the informal sector and expanding social security benefits to people in that sector. The challenge is to design and operate programs that are well targeted and fiscally sustainable.

The cabinet has approved in principle the establishment of a Post Bank, using the post office network to provide low-interest loans of up to B10,000 ($330). Other microfinance arrangements are under consideration to assist low-income households.

Additionally, the government plans to distribute community land-title deeds to more than 200,000 landless people and farmers living on plots owned by the state.